VIEWPOINT

Pension Review: Balancing innovation over scale

MUFG Retirement Solutions, in the UK, recently responded to His Majesty's Government on its Pension scheme investments review, a significant initiative aiming to boost investment, increase saver returns and reduce inefficiencies in the pensions system.

With over 2.1 million pension members in UK master trusts and defined benefit arrangements, and more than 12.5 million members globally, MUFG Retirement Solutions is well positioned to contribute valuable insights to this discussion.

The interim report, published on 14 November 2024, outlined key proposals on scaling pension schemes, consolidating funds, and leveraging pension investments for UK economic growth. Additionally, it introduced recommendations for the local government pension scheme focused on pooling assets and strengthening governance.

MUFG's response highlighted the following key points:

The Risks of Artificial Scale Targets

While achieving scale in the pensions market is important, we believe scale targets are less meaningful as they represent a single point in time rather than ongoing value creation. Imposing artificial scale "hurdles" risks unintended consequences that could harm members, discourage competition and stifle innovation.

The UK Defined Contribution (DC) market has thrived thanks to significant technological and investment innovations introduced by startups, which have showcased the potential of UK private companies. Government interventions should be cautious not to limit future disruptors that drive our capacity for innovation and progress.

The Benefits of Smaller and Agile Market Participants

New and innovative providers have demonstrated how thinking differently and challenging the status quo can lead to better member outcomes. We must acknowledge the risks of diseconomies of scale, where excessive growth can reduce operational efficiency and flexibility, and be potentially harmful.

Scale need not be concentrated within individual providers. Collaborative approaches, such as co-investment or leveraging scale at the fund level (e.g. LTAFs), can capture the benefits of scale without the risks of centralised growth. This is a model has proven successful in other jurisdictions, like Australia.

Investment in UK Private Assets and Infrastructure

Increased investment in UK-based private assets, such as private capital and infrastructure, does not necessarily require large-scale providers. The government should clarify its objectives and consider alternative methods to drive its desired outcomes. Mandating allocations to specific asset classes or adopting a "comply or explain" framework could achieve results faster and with less risk than current proposals. These approaches would simplify member communication, fostering greater understanding and trust.

Consolidation of Default Arrangements

We recognise the merit in consolidating default arrangements, especially when legacy defaults have disadvantaged members or stretched governance resources. However, a one-size-fits-all approach may not be appropriate. As technology advances, the potential for more personalised default strategies, built using common components, should be considered.

Addressing Cost Versus Value

The UK pensions market has long prioritised cost over value, to the detriment of member outcomes. We support the introduction of a single price mechanism to ensure greater equity among pension scheme members. By removing disparities tied to employer bargaining power or advisory resources, a single price model will create a fairer system and ultimately deliver better outcomes for all.

Enhancing the Attractiveness of UK Investments

To create a more competitive environment in the UK, the government must address factors currently deterring investors and IPO prospects. For example, the barrier created by stamp duty on UK public markets requires review to ensure a more competitive investment environment. Similarly, adopting positive incentives for holding UK shares, such as the "franking credits" seen in Australia, could encourage greater investment and bolster the attractiveness of the UK as a financial hub.

While we support the government's commitment to reforming the DC pensions market, we urge a balanced and thoughtful approach that considers the complexities of scale targets and the broader opportunities for driving innovation, competition, and investment. A well-designed strategy can lay the foundation for a more resilient and equitable pensions market that delivers financial security for millions while contributing to sustainable economic growth.

MUFG Retirement Solutions remains dedicated to engaging with policymakers, clients and industry stakeholders to develop solutions that drive better outcomes for members, the pensions sector and the broader UK economy.

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